Sales type code means the contract type or general disposition (e.g., arm's-length or non-arm's-length) of production from the lease. The sales type code applies to the sales contract, or other disposition, and not to the arm's-length or non-arm's-length nature of a transportation or processing allowance.

Spot sales agreement means a contract wherein a seller agrees to sell to a buyer a specified amount of unprocessed gas, residue gas, or gas plant products at a specified price over a fixed period, usually of short duration. It also does not normally require a cancellation notice to terminate, and does not contain an obligation, or imply an intent, to continue in subsequent periods.

Takes means when the operating rights owner sells or removes production from, or allocated to, the lease, or when such sale or removal occurs for the benefit of an operating rights owner.

Work-back method means the same as net-back method.

[64 FR 43515, Aug. 10, 1999, as amended at 73 FR 15891, Mar. 26, 2008]

§ 1206.172 How do I value gas produced from leases in an index zone?

(a) *What leases this section applies to.* This section explains how lessees must value, for royalty purposes, gas produced from Indian leases located in an index zone. For other leases, value must be determined under § 1206.174.

(1) You must use the valuation provision of this section if your lease is in an index zone and meets one of the following two requirements:

(i) Has a major portion provision;

(ii) Does not have a major portion provision, but provides for the Secretary to determine the value of production.

(2) This section does not apply to carbon dioxide, nitrogen, or other non-hydrocarbon components of the gas stream. However, if they are recovered and sold separately from the gas stream, you must determine the value of these products under § 1206.174.

(b) *Valuing residue gas and gas before processing.* (1) Except as provided in paragraphs (e), (f), and (g) of this section, this paragraph (b) explains how you must value the following four types of gas:

(i) Gas production before processing;

(ii) Gas production that you certify on Form MMS–4410, Certification for Not Performing Accounting for Comparison (Dual Accounting), is not processed before it flows into a pipeline with an index but which may be processed later;

(iii) Residue gas after processing; and

(iv) Gas that is never processed.

(2) The value of gas production that is not sold under an arm's-length dedicated contract is the index-based value determined under paragraph (d) of this section unless the gas was subject to a previous contract which was part of a gas contract settlement. If the previous contract was subject to a gas contract settlement and if the royalty-bearing contract settlement proceeds per MMBtu added to the 80 percent of the safety net prices calculated at § 1206.172(e)(4)(i) exceeds the index-based value that applies to the gas under this section (including any adjustments required under § 1206.176), then the value of the gas is the higher of the value determined under this section (including any adjustments required under § 1206.176) or § 1206.174.

(3) The value of gas production that is sold under an arm's-length dedicated contract is the higher of the index-based value under paragraph (d) of this section or the value of that production determined under § 1206.174(b).

(c) *Valuing gas that is processed before it flows into a pipeline with an index.* Except as provided in paragraphs (e), (f), and (g) of this section, this paragraph (c) explains how you must value gas that is processed before it flows into a pipeline with an index. You must value this gas production based on the higher of the following two values:

(1) The value of the gas before processing determined under paragraph (b) of this section.

(2) The value of the gas after processing, which is either the alternative dual accounting value under § 1206.173 or the sum of the following three values:

(i) The value of the residue gas determined under paragraph (b)(2) or (3) of this section, as applicable;

(ii) The value of the gas plant products determined under § 1206.174, less any applicable processing and/or transportation allowances determined under this subpart; and

(iii) The value of any drip condensate associated with the processed gas determined under subpart B of this part.

(d) *Determining the index-based value for gas production.* (1) To determine the index-based value per MMBtu for production from a lease in an index zone, you must use the following procedures:

(i) For each ONRR-approved publication, calculate the average of the highest reported prices for all index-pricing points in the index zone, except for any prices excluded under paragraph (d)(6) of this section;

(ii) Sum the averages calculated in paragraph (d)(1)(i) of this section and divide by the number of publications; and

(iii) Reduce the number calculated under paragraph (d)(1)(ii) of this section by 10 percent, but not by less than 10 cents per MMBtu or more than 30 cents per MMBtu. The result is the index-based value per MMBtu for production from all leases in that index zone.

(2) ONRR will publish in the FEDERAL REGISTER the index zones that are eligible for the index-based valuation method under this paragraph. ONRR will monitor the market activity in the index zones and, if necessary, hold a technical conference to add or modify a particular index zone. Any change to the index zones will be published in the FEDERAL REGISTER. ONRR will consider the following five factors and conditions in determining eligible index zones:

(i) Areas for which ONRR-approved publications establish index prices that accurately reflect the value of production in the field or area where the production occurs;

(ii) Common markets served;

(iii) Common pipeline systems;

(iv) Simplification; and

(v) Easy identification in ONRR's systems, such as counties or Indian reservations.

(3) If market conditions change so that an index-based method for determining value is no longer appropriate for an index zone, ONRR will hold a technical conference to consider disqualification of an index zone. ONRR will publish notice in the FEDERAL REGISTER if an index zone is disqualified. If an index zone is disqualified, then production from leases in that index zone cannot be valued under this paragraph.

(4) ONRR periodically will publish in the FEDERAL REGISTER a list of acceptable publications based on certain criteria, including, but not limited to the following five criteria:

(i) Publications buyers and sellers frequently use;

(ii) Publications frequently referenced in purchase or sales contracts;

(iii) Publications that use adequate survey techniques, including the gathering of information from a substantial number of sales;

(iv) Publications that publish the range of reported prices they use to calculate their index; and

(v) Publications independent from DOI, lessors, and lessees.

(5) Any publication may petition ONRR to be added to the list of acceptable publications.

(6) ONRR may exclude an individual index price for an index zone in an ONRR-approved publication if ONRR determines that the index price does not accurately reflect the value of production in that index zone. ONRR will publish a list of excluded indices in the FEDERAL REGISTER.

(7) ONRR will reference which tables in the publications you must use for determining the associated index prices.

(8) The index-based values determined under this paragraph are not subject to deductions for transportation or processing allowances determined under §§ 1206.177, 1206.178, 1206.179, and 1206.180.

(e) *Determining the minimum value for royalty purposes of gas sold beyond the first index pricing point.* (1) Notwithstanding any other provision of this section, the value for royalty purposes of gas production from an Indian lease that is sold beyond the first index pricing point through which it flows cannot be less than the value determined under this paragraph (e).

(2) By June 30 following any calendar year, you must calculate for each

month of that calendar year your safety net price per MMBtu using the procedures in paragraph (e)(3) of this section. You must calculate a safety net price for each month and for each index zone where you have an Indian lease for which you report and pay royalties.

(3) Your safety net price (S) for an index zone is the volume-weighted average contract price per delivered MMBtu under your or your affiliate's arm's-length contracts for the disposition of residue gas or unprocessed gas produced from your Indian leases in that index zone as computed under this paragraph (e)(3).

(i) Include in your calculation only sales under those contracts that establish a delivery point beyond the first index pricing point through which the gas flows, and that include any gas produced from or allocable to one or more of your Indian leases in that index zone, even if the contract also includes gas produced from Federal, State, or fee properties. Include in your volume-weighted average calculation those volumes that are allocable to your Indian leases in that index zone.

(ii) Do not reduce the contract price for any transportation costs incurred to deliver the gas to the purchaser.

(iii) For purposes of this paragraph (e), the contract price will not include the following amounts:

(A) Any amounts you receive in compromise or settlement of a predecessor contract for that gas;

(B) Deductions for you or any other person to put gas production into marketable condition or to market the gas; and

(C) Any amounts related to marketable securities associated with the sales contract.

(4) Next, you must determine for each month the safety net differential (SND). You must perform this calculation separately for each index zone.

(i) For each index zone, the safety net differential is equal to: $SND = [(0.80 \times S) - (1.25 \times I)]$ where (I) is the index-based value determined under 30 CFR 206.172(d).

(ii) If the safety net differential is positive you owe additional royalties.

(5)(i) To calculate the additional royalties you owe, make the following calculation for each of your Indian leases in that index zone that produced gas that was sold beyond the first index-pricing point through which the gas flowed and that was used in the calculation in paragraph (e)(3) of this section:

Lease royalties owed = $SND \times V \times R$, where R = the lease royalty rate and V = the volume allocable to the lease which produced gas that was sold beyond the first index pricing point.

(ii) If gas produced from any of your Indian leases is commingled or pooled with gas produced from non-Indian properties, and if any of the combined gas is sold at a delivery point beyond the first index pricing point through which the gas flows, then the volume allocable to each Indian lease for which gas was sold beyond the first index pricing point in the calculation under paragraph (e)(5)(i) of this section is the volume produced from the lease multiplied by the proportion that the total volume of gas sold beyond the first index pricing point bears to the total volume of gas commingled or pooled from all properties.

(iii) Add the numbers calculated for each lease under paragraph (e)(5)(i) of this section. The total is the additional royalty you owe.

(6) You have the following responsibilities to comply with the minimum value for royalty purposes:

(i) You must report the safety net price for each index zone to ONRR on Form MMS–4411, Safety Net Report, no later than June 30 following each calendar year;

(ii) You must pay and report on Form MMS–2014 additional royalties due no later than June 30 following each calendar year; and

(iii) ONRR may order you to amend your safety net price within one year from the date your Form MMS–4411 is due or is filed, whichever is later. If ONRR does not order any amendments within that one-year period, your safety net price calculation is final.

(f) *Excluding some or all tribal leases from valuation under this section.* (1) An Indian tribe may ask ONRR to exclude some or all of its leases from valuation under this section. ONRR will consult with BIA regarding the request.

(i) If ONRR approves the request for your lease, you must value your production under §1206.174 beginning with production on the first day of the second month following the date ONRR publishes notice of its decision in the FEDERAL REGISTER.

(ii) If an Indian tribe requests exclusion from an index zone for less than all of its leases, ONRR will approve the request only if the excluded leases may be segregated into one or more groups based on separate fields within the reservation.

(2) An Indian tribe may ask ONRR to terminate exclusion of its leases from valuation under this section. ONRR will consult with BIA regarding the request.

(i) If ONRR approves the request, you must value your production under §1206.172 beginning with production on the first day of the second month following the date ONRR publishes notice of its decision in the FEDERAL REGISTER.

(ii) Termination of an exclusion under paragraph (f)(2)(i) of this section cannot take effect earlier than 1 year after the first day of the production month that the exclusion was effective.

(3) The Indian tribe's request to ONRR under either paragraph (f)(1) or (2) of this section must be in the form of a tribal resolution.

(g) *Excluding Indian allotted leases from valuation under this section.* (1)(i) ONRR may exclude any Indian allotted leases from valuation under this section. ONRR will consult with BIA regarding the exclusion.

(ii) If ONRR excludes your lease, you must value your production under §1206.174 beginning with production on the first day of the second month following the date ONRR publishes notice of its decision in the FEDERAL REGISTER.

(iii) If ONRR excludes any Indian allotted leases under this paragraph (g)(1), it will exclude all Indian allotted leases in the same field.

(2)(i) ONRR may terminate the exclusion of any Indian allotted leases from valuation under this section. ONRR will consult with BIA regarding the termination.

(ii) If ONRR terminates the exclusion, you must value your production under §1206.172 beginning with production on the first day of the second month following the date ONRR publishes notice of its decision in the FEDERAL REGISTER.

§1206.173 How do I calculate the alternative methodology for dual accounting?

(a) *Electing a dual accounting method.* (1) If you are required to perform the accounting for comparison (dual accounting) under §1206.176, you have two choices. You may elect to perform the dual accounting calculation according to either §1206.176(a) (called actual dual accounting), or paragraph (b) of this section (called the alternative methodology for dual accounting).

(2) You must make a separate election to use the alternative methodology for dual accounting for your Indian leases in each ONRR-designated area. Your election for a designated area must apply to all of your Indian leases in that area.

(i) ONRR will publish in the FEDERAL REGISTER a list of the lease prefixes that will be associated with each designated area for purposes of this section. The ONRR-designated areas are as follows:

(A) Alabama-Coushatta;
(B) Blackfeet Reservation;
(C) Crow Reservation;
(D) Fort Belknap Reservation;
(E) Fort Berthold Reservation;
(F) Fort Peck Reservation;
(G) Jicarilla Apache Reservation;
(H) ONRR-designated groups of counties in the State of Oklahoma;
(I) Navajo Reservation;
(J) Northern Cheyenne Reservation;
(K) Rocky Boys Reservation;
(L) Southern Ute Reservation;
(M) Turtle Mountain Reservation;
(N) Ute Mountain Ute Reservation;
(O) Uintah and Ouray Reservation;
(P) Wind River Reservation; and
(Q) Any other area that ONRR designates. ONRR will publish a new area designation in the FEDERAL REGISTER.

(ii) You may elect to begin using the alternative methodology for dual accounting at the beginning of any month. The first election to use the alternative methodology will be effective from the time of election through the end of the following calendar year.